FINRA Streamlines Clearance Process for Certain Shelf Offerings Benefiting Smaller Issuers

Effective March 1, 2010, the Financial Industry Regulatory Authority (FINRA) announced a new approval process whereby underwriters and placement agents may utilize a “Same Day Clearance” procedure to obtain the requisite clearance from FINRA prior to the launch of certain offerings made from shelf registration statements, thereby enabling some smaller issuers to access market opportunities more efficiently. However, this procedure is not available for all shelf offerings, and, in some cases, may not be in an issuer’s best interest to utilize.

Filing Requirement

FINRA regulates the terms and arrangements of its members’ activities distributing securities for the benefit of issuers and the investing public. Under FINRA Rule 5110, FINRA must review and approve the underwriting or placement agent compensation and other arrangements in certain registered offerings, which includes receipt of a variety of representations regarding compensation, conflicts of interest and relationships between the issuer, its insiders and FINRA members, and a review of all deal-related documentation. Although there are limited exceptions from this requirement, primarily related to the size of the issuer’s public float or the type of securities offered, most registered equity offerings by issuers with a public float of less than $150 million require receipt of a “Conditional No Objections Notice” from FINRA prior to sale of securities off a shelf registration statement (i.e., clearance to proceed on the terms disclosed to FINRA), and receipt of a final “No Objections Notice” upon completion of the offering. Generally, receipt of a Conditional No-Objections Notice could take between two to three weeks from the time of initial filing with FINRA, or longer for offerings with complex compensation structures.

Same Day Clearance Procedure

The new Same Day Clearance procedure provides for immediate receipt of a Conditional No Objections Notice, if the FINRA filing is successfully submitted before 4:00 p.m. ET on any given business day through COBRADesk, FINRA’s online filing system. If the filing is not successfully accepted through COBRADesk prior to 4:00 p.m. ET, the Conditional No Objections Notice will not issue until the

2 Most offerings by larger issuers rely on an exemption from Rule 5110 that provides that issuers who were eligible to use Form S-3 or F-3 based on the eligibility requirements in effect prior to October 21, 1992 may complete shelf offerings from registration statements on such forms without a FINRA filing and clearance pursuant to Rule 5110. Under this requirement, an issuer must have been subject to SEC reporting requirements for at least 3 years and be current in its reporting obligations and either (i) have a public float of $150 million (or $300 million for issuers using Form F-3) or (ii) have a public float between $100 million and $150 million and have an annual trading volume of 3 million shares. See Rule 5110(b)(7) and (8) for this and other exemptions.
following day upon acceptance of the filing. The Same Day Clearance procedure is available for obtaining clearance on base filings, takedown filings or “concurrent filings,” encompassing both the base prospectus and the proposed takedown.

To obtain a Same Day Clearance, the filing party must make certain representations regarding the issuer and its and its insiders’ relationships with FINRA members and the proposed offering. These representations include that:

For a Base Filing:

- The appropriate sections of the base prospectus disclose the aggregate value of all compensation anticipated to be received by participating FINRA members in any offering from the shelf registration statement, and that such compensation shall not exceed 8% of any offering proceeds (as calculated pursuant to FINRA Rule 5110), or that such disclosure will be included in any post-effective amendment.

- In the event the offering is subject to NASD Rule 2720 (which governs conflicts of interest of FINRA members and dictates situations in which a “qualified independent underwriter,” or “QIU,” must be involved in the offering), the base prospectus complies with the applicable prominent disclosure provisions of NASD Rule 2720.¹

- The filer’s representations are accurate and the filer understands that the filing will be subject to post-offering review and verification by FINRA.

For a Takedown Filing:

- The terms and arrangements between participating FINRA members and the issuer do not include any prohibited arrangements as described in FINRA Rule 5110(f)(2).²

- The aggregate value of all items of compensation received or to be received by participating FINRA members in connection with the takedown offering does not exceed 8% of the offering proceeds and that all such compensation and the terms and arrangements entered into by the participating FINRA members and the issuer are disclosed in the form of prospectus related to distribution of this offering.

- Participating FINRA members have not acquired unregistered securities that would be deemed underwriting compensation during the 180-day period preceding the filing. Note, although FINRA has not yet published formal guidance on the new Same Day Clearance procedure, the FINRA staff has provided informal guidance that this representation is interpreted to include any proposed securities to be issued in conjunction with the offering to participating FINRA members, and thus effectively limits the Same Day Clearance procedure to offerings with only cash compensation for FINRA members.

- In the event Rule 2720(a)(2) applies to the offering, the QIU is one whose qualifications have been approved by FINRA within the prior 12-month period.

- The final offering documents, signed agreements related to the offering (including letters of intent or engagement letters) and other documents entered into by any participating FINRA member and the issuer in the 180-day period prior to the filing will be submitted to COBRADesk, and specified additional information prior to making this representation. Prohibited arrangements include, but are not limited to, certain types of accountable expenses, any non-accountable expense allowance in excess of 3% of offering proceeds, certain types of advance payments to FINRA members, certain payments in conjunction with incomplete or aborted offerings, certain “tail fee” arrangements, certain rights of first refusal or payments for waivers thereof, securities with certain anti-dilution and/or registration rights, and any over-allotment option of more than 15% in a firm commitment offering.

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² Issuers and FINRA members should carefully review the terms and arrangements listed in Rule 5110(f)(2) as prohibited.
required in COBRADesk will be completed.

- The filer’s representations are accurate and the filer understands that the filing will be subject to post-offering review and verification by FINRA.

For a takedown filing, the filer must also identify the participating FINRA members in the offering. For a concurrent filing, the filer must make both sets of these representations and identify the participating FINRA member(s).

**Key Considerations for Use of the Same Day Clearance Procedure**

- The Same Day Clearance procedure does not change the FINRA rules applicable to shelf offerings and the issuer and participating FINRA members will still be required to provide FINRA the same overall information.

- As the new Same Day Clearance procedure requires a series of representations, issuers and FINRA members should still gather and analyze the information required for a full COBRADesk filing as soon as possible in the offering process, to ensure that the filer can accurately assess whether the required representations can be made for the Same Day Clearance process, to ensure that any QIU-related requirements can be timely and fully met and to address basic conflicts and compensation related disclosure concerns in the issuer’s base prospectus and prospectus supplement, as applicable.

- To use the Same Day Clearance procedure, the items of compensation received or to be received by participating FINRA members in connection with the offering may only consist of cash and may not include any securities.

- As each filing under the Same Day Clearance procedure is subject to further review and verification by FINRA, it is possible that the FINRA staff will issue post-offering comments and seek further information post-offering. To the extent that the FINRA staff find that any of the representations made in the Same Day Clearance process are inaccurate or otherwise determine that the terms and arrangements and/or disclosure documentation are not fully compliant with applicable rules, FINRA may require that the terms and arrangements be unwound or adjusted and/or that the issuer amend or correct its disclosure to reach compliance. Such post-offering changes or additional disclosure could be disruptive to the issuer’s trading market and could raise questions regarding the adequacy of the issuer’s offering disclosures at time of sale of the securities. If a filer is uncertain about eligibility for use of the Same Day Clearance procedure or whether proposed non-customary terms or arrangements (for example, sharing of compensation with a non-participating FINRA member, waiver of a prior tail provision, etc.) and related disclosures are compliant with FINRA rules, the parties should seek FINRA feedback prior to filing or utilize the regular filing procedures, which will allow the issuer to receive feedback from FINRA and make any required adjustments to the terms, arrangements and/or planned disclosure prior to the offering and sale of the securities, thereby avoiding the risk of subsequent disruptive changes.

FINRA has indicated that it intends to publish further guidance on the Same Day Clearance procedure, which issuers and FINRA members should review when available.
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